

## DECENTRALIZATION SUPPORT PROGRAM

(EC-0204)

### EXECUTIVE SUMMARY

<b>Borrower and guarantor:</b>	Government of Ecuador	
<b>Executing agency:</b>	Consejo Nacional de Modernización del Estado [National Council on Modernization of the State] (CONAM)	
<b>Amount and source:</b>	IDB (OC):	US\$4.8 million
	Local:	US\$1.2 million
	Total:	US\$6.0 million
<b>Financial terms and conditions:</b>	Amortization period:	25 years
	Grace period:	4.5 years
	Disbursement period:	4 years
	Interest rate:	variable (IFF)
	Inspection and supervision:	1%
	Credit fee:	0.75%
	Currency:	U.S. dollars, Single Currency Facility
<b>Objectives:</b>	<p>Through technical assistance and training, the program will support decentralization and the transfer of responsibilities to sectional governments in Ecuador. It will also support updating of the legal and financial framework for fiscal decentralization.</p> <p>The specific objectives of the operation are: (a) development of a legislative and institutional framework for decentralization; (b) support for implementing the annual decentralization plans approved by the government that put into effect the gradual transfer of powers to the sectional governments; (c) preparation of legislative reforms to consolidate the regulatory framework governing the country's subnational organization, financing for the sectional governments and local taxation into a single system; and (d) studies and proposals reached by consensus with interested sectors to entrench the reforms in subnational organization, giving special consideration to reforms of the autonomous regime and organization of districts for indigenous and Afro-Ecuadorian communities.</p>	

**Description:** The program consists of the four components described below.

**Component 1. Support for implementation of decentralization** (US\$3.3 million). This component will support: (a) the development and consolidation of the legislative and institutional framework for subnational organization and decentralization; (b) the transfer processes established in the first three annual decentralization plans; (c) strengthening of the ministries of the central and sectional governments involved in the negotiations for the effective transfer of powers; and (d) the establishment of coordination mechanisms for public policy formulation in the framework of the new institutional system created by decentralization.

**Component 2. Support for fiscal decentralization** (US\$450,000). The purpose of this component is to help refine the current subnational fiscal management model. Loan proceeds will be used to support the Ecuadorian government in the design of alternative formulae to improve the current framework and deepen fiscal decentralization in a prudent manner, maintaining macroeconomic balances and providing the funds and controls needed to enable the sectional governments to carry out their new functions adequately. This component will be developed jointly with the Ministry of Economic Affairs and Finance and includes: (a) studies to prepare alternative models for financing the sectional governments; (b) actions to strengthen the local tax administrations; (c) studies and proposals on the implementation of cofinancing mechanisms; and (d) design of information systems for decentralization and monitoring and control of the finance and performance of sectional governments.

**Component 3. Studies** (US\$380,000). The program will finance studies on the physical delimitation of special indigenous and Afro-Ecuadorian districts, with a view to generating technically grounded justified legislative proposals, arrived at by consensus with the interested parties.

The component will also finance the commissioning of studies aimed at deepening the process leading to autonomy in Ecuador, taking into account its impact on governance and fiscal management.

**Component 4. Citizen communication and social participation** (US\$640,000). This component will support the process of public information and citizen oversight to follow the progress of fiscal and administrative decentralization through: (a) monitoring of public opinion; (b) citizen communication activities; and (c) promotion of social participation.

**The Bank's  
country and  
sector strategy:**

The Bank's strategy in Ecuador gives priority to the following: (a) better governance and the quest for mechanisms to overcome political and regional fragmentation; (b) economic stabilization; (c) modernization of the public sector; (d) recovery and growth in physical and human capital; and (e) social and ethnic inclusion. A new subnational development strategy has recently been approved, based on the following intervention criteria: (a) cross-cutting basic institutional requirements in the transfer process to avoid undesirable inequity and disparities in delivery of the transferred services; (b) control of the fiscal impact; (c) priority development of the capacity of the sectional governments to meet the needs of the population in relevant sectors; (d) flexibility of the process of the devolution of powers, that must be adapted to the differences in capacity and will of the sectional governments; and (e) gradualism in the transfer of responsibilities for service delivery in terms of existing institutional capacity in the sectional governments. The Bank has assisted the Ecuadorian government and the executing agency with technical and financial support to implement the initial actions in the institutionalization and development of the decentralization process and the formation of a team of local specialists who have advised the government on the ramifications of the process. The specialists have cooperated with different ministries in organizing their own technical teams to undertake negotiations and reach agreements on the transfer of powers.

**Environmental  
and social  
review:**

Decentralization will lead to improvements in social equity, through greater efficiency and transparency in the allocation of fiscal resources and fairer distribution of them. Alternatives to the current rules governing subnational organization, local taxation and intergovernmental transfers will be studied, to find more effective and equitable fiscal solutions, linked to the differences in tax potential in local communities. The program will carry out activities with community leaders and civil society organizations to explain the scope of the decentralization reform and the new responsibilities of local communities once powers have actually been transferred. The studies on the physical boundaries of indigenous and Afro-Ecuadorian districts will channel the demands that have been embodied in the constitution but have not yet been met.

With respect to institutional systems for environmental management and protection, the program will finance actions to strengthen the Ministry of the Environment in the areas of regulatory functions and the development of standards and systems for monitoring and control of the environmental responsibilities that are transferred. It will strengthen the systems that evaluate the environmental capacity of the sectional governments and provide technical assistance to build it up.

The country has guidelines for environmental management and protection for the main urban and municipal services, that were developed with Bank support under the global credit program for municipal development.

**Benefits:**

The program will support an institutional and social process to comply with constitutional commitments and laws that were passed with broad popular and political consensus but which have not been implemented owing to the lack of an appropriate framework for governance and clear procedures for transferring powers. The program will promote the efficiency, transparency and equity of the distribution of public funds to the local levels and strengthen local decision making and accountability. It will also improve the legal and regulatory framework for subnational governments and fiscal decentralization in Ecuador and will provide a technically grounded reasoned response to the possibility of establishing special indigenous and Afro-Ecuadorian districts.

The program will be framed in a new strategy of fiscal discipline and accountability that will be applied to all levels of government, including the budget management of the sectional governments themselves. It is expected that the sectional tax reform and support for strengthening the municipal tax administrations will contribute positively to local financial autonomy.

**Risks:**

All decentralization processes are strongly conditioned by the political context. Therefore, an operation of this kind is subject to some uncertainty with regard to its final outcome. Like other major challenges facing the country, decentralization requires continued work on building political and institutional consensuses, which are indispensable for the feasibility of a proposal of this kind. However, the measure of success will be to inaugurate the process and make progress in transferring responsibilities, while ensuring that certain minimum criteria are complied with to provide continuity and the capacity to manage the services transferred. The country's fiscal precariousness is another important determining factor and therefore the plan must progress in step with the central and sectional governments' capacity to effectively comply with the

financial commitments made in each transfer negotiation. The results of the elections to be held within less than two years add uncertainty to the project execution period, and therefore a mid-term evaluation has been planned, when the new government takes office.

The program's execution is complex. To address this problem, quarterly reprogramming and semiannual evaluations of progress have been planned, to be performed by the Bank, the borrower and the executing agency, with support from international consultants. A complete timetable of activities has been prepared up to the mid-term evaluation, which will take place 18 months after the program begins. The timing and number of open calls for proposals and tender calls for services have been simplified to facilitate the launch of the program, its monitoring and Bank supervision.

**Special  
contractual  
clauses:**

The following are conditions precedent to the first disbursement:

- a. Establishment of the executing unit and appointment of the general coordinator and staff (see paragraph 3.3); and
- b. Selection, with the Bank's nonobjection, of the international consultants to take charge of advisory services for reprogramming targets and following up on the program (see paragraph 3.7).

**Other special contractual obligations:**

- a. Within the three months following the date of the first disbursement, the international consultants who will be in charge of advising on target reprogramming and program follow-up will have been hired.
- b. Within the six months following entry into force of the loan contract, the joint commissions in at least four ministries will have been set up (see paragraph 2.6).
- c. The executing agency will sign agreements with the Ministry of Economic Affairs and Finance (MEF), the Association of Ecuadorian Municipalities (AME), the Consortium of Provincial Councils of Ecuador (CONCOPE), the Council for the Development of Ecuador's Nationalities and Peoples (CODENPE) and the GTZ to assure their participation in the execution or supervision of specific program activities. The Bank will review the agreements and give its nonobjection prior to committing funding for the respective component or activity (see paragraph 3.4).

<b>Poverty-targeting and social sector classification:</b>	This operation does not qualify as a social equity enhancing project, as described in the indicative targets mandated by the Bank's Eighth Replenishment (document AB-1704). Furthermore, this operation does not qualify as a poverty-targeted investment (PTI).
<b>Exceptions to Bank policy:</b>	None
<b>Procurement:</b>	The thresholds applicable to Ecuador are US\$250,000 for the procurement of goods and services and US\$200,000 for consulting services. Procurements of goods and services with reference prices between US\$100,000 and US\$250,000 will be made under local competitive bidding and local shopping will be used under US\$100,000. Consulting services with reference prices under US\$200,000 will be based on prequalification of consulting firms and direct invitations to firms on the short list prepared by the executing agency.